

COCHISE HEALTH SYSTEMS

Financial Statements

and

Supplemental Information

June 30, 2011

CONTENTS

	<u>Page</u>
Independent Auditors' Report	1
Financial Statements	
Statement of Net Assets – Enterprise Fund	2
Statement of Revenues, Expenses, and Changes in Net Assets – Enterprise Fund	3-5
Statement of Cash Flows – Enterprise Fund	6
Notes to Financial Statements	7-13
Supplemental Information	
Report #1 – Statement of Financial Position, Net Assets or Balance Sheet	14
Report #2 – Statement of Activities/Income Statements	15-16
Report #3 – Investments and Balance Sheet “Other Account” Details	17
Report #4 – Income Statement “Other Account” Details	18
Report #6 – Claims Lag Report for Prospective Period Only-IBNR	19
Report #7 – Utilization Data Report	20
Report #8 – FQHC Reasonable Cost Reimbursement	21
List of Plan Officers and Directors	22

Fester & Chapman P.C.

Certified
Public
Accountants

4001 North 3rd Street
Suite 275
Phoenix, AZ 85012-2086

Tel: (602) 264-3077
Fax: (602) 265-6241

Independent Auditors' Report

The Board of Supervisors of
Cochise County, Arizona

We have audited the accompanying financial statements of Cochise Health Systems (the Plan), a proprietary fund of Cochise County, Arizona, as of and for the year ended June 30, 2011, as listed in the table of contents. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only Cochise Health Systems and do not purport to, and do not, present fairly the financial position of Cochise County, Arizona, as of June 30, 2011, and the changes in its financial position, or, where applicable, its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Cochise Health Systems as of June 30, 2011, and the changes in its financial position and cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

Our audit was made for the purpose of forming an opinion on the basic financial statements of the Plan taken as a whole. The accompanying supplemental information is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Fester & Chapman P.C.

February 1, 2012

Cochise Health Systems

STATEMENT OF NET ASSETS
ENTERPRISE FUND

June 30, 2011

ASSETS

Current assets:

Cash and cash equivalents	\$ 5,613,356
Reinsurance receivable	686,380
Capitation and reconciliations receivable	<u>191,019</u>
Total current assets	6,490,755

Noncurrent assets:

Capital assets:

Furniture, equipment and vehicles	122,024
Accumulated depreciation	<u>(98,353)</u>
	<u>23,671</u>

Total assets	<u>6,514,426</u>
--------------	------------------

LIABILITIES AND NET ASSETS

Current liabilities:

AHCCCS member care liabilities	3,066,700
Accounts payable	209,443
Accrued payroll and related expenses	<u>166,111</u>
Total current liabilities	3,442,254

Net assets:

Invested in capital assets	23,671
Restricted for health care	1,738,000
Unrestricted	<u>1,310,501</u>
Total net assets	<u>\$ 3,072,172</u>

The accompanying notes are an integral part of this statement.

Cochise Health Systems

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
ENTERPRISE FUND

Year Ended June 30, 2011

Operating revenues:

Capitation and share of cost reconciliation	\$ 32,168,861
Reinsurance	1,365,236
HCBS placement reconciliation	109,230
Patient contributions	22,903
Third party liability	4,531
Other	<u>9,948</u>
Total operating revenues	33,680,709

Operating expenses:

Acute care:

Hospitalization	1,230,974
Primary care physician	278,296
Outpatient facility	235,590
Referral physician services	371,859
Pharmacy	422,563
Lab and radiology	143,921
Transportation	788,059
Therapies	56,214
Emergency services	179,965
Durable medical equipment	300,606
Outpatient behavioral health	98,303
PPC acute care	21,010
Dental	11,681
Other acute care costs	<u>4,055</u>
Total acute care	<u>4,143,096</u>

Institutional care:

Nursing home ICF and bedholds	7,941,606
SNF Level I	5,038,889
SNF Level II	1,243,765
SNF Level III	1,280,078
Institutional care	425,619
PPC institutional expenses	<u>213,454</u>
Total institutional care	<u>16,143,411</u>

(Continued)

The accompanying notes are an integral part of this statement.

Cochise Health Systems

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
ENTERPRISE FUND

Year Ended June 30, 2011
(Continued)

Home and community based services:

Home health nurse	\$ 365,130
Personal care	123,465
Homemaker	41,529
Home delivered meals	109,219
Respite care	21,372
Attendant care	4,161,698
Assisted living in-home	887,712
Adult foster care	156,836
Environmental modifications	43,208
Assisted living center	745,888
Other HCBS	31,323
PPC HCBS	41,666
Total home and community based services	<u>6,729,046</u>

Case management:

Case management payroll and payroll related	1,325,866
Case management, other	<u>23,963</u>
Total case management	<u>1,349,829</u>

Total medical expenses	<u>28,365,382</u>
------------------------	-------------------

(Continued)

The accompanying notes are an integral part of this statement.

Cochise Health Systems

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
ENTERPRISE FUND

Year Ended June 30, 2011
(Continued)

Administration expenses:	
Administrative payroll and payroll related	\$ 1,535,565
Data processing	144,000
Professional fees	48,349
Occupancy	9,495
Other	951,346
Depreciation	<u>11,755</u>
Total administration expenses	<u>2,700,510</u>
Total operating expenses	<u>31,065,892</u>
Operating income	2,614,817
Nonoperating revenues (expenses)	
Loss on disposal of assets	(10,963)
Interest income	100,033
Premium tax	<u>(661,263)</u>
Total nonoperating revenues (expenses), net	<u>(572,193)</u>
Income before transfers	2,042,624
Transfers to Cochise County	<u>(8,599,225)</u>
Decrease in net assets	(6,556,601)
Total net assets, July 1, 2010	<u>9,628,773</u>
Total net assets, June 30, 2011	<u>\$ 3,072,172</u>

The accompanying notes are an integral part of this statement.

Cochise Health Systems

STATEMENT OF CASH FLOWS
ENTERPRISE FUND

Year Ended June 30, 2011

Cash flows from operating activities:	
Cash received from:	
Contractors, patients, and other payors	\$ 33,282,578
Miscellaneous operations	35,232
Cash payments to:	
Providers for health care services	(27,524,422)
Suppliers for goods and services	(1,121,776)
Employees for services	<u>(2,923,461)</u>
Net cash provided by operating activities	1,748,151
Cash flows from noncapital financing activities:	
Cash transfers to other Cochise County funds	(8,599,225)
Premium tax payments	<u>(661,263)</u>
Net cash used for noncapital financing activities	(9,260,488)
Cash flows from investing activities:	
Interest received on cash and cash equivalents	<u>100,033</u>
Net cash provided by investing activities	<u>100,033</u>
Net decrease in cash and cash equivalents	(7,412,304)
Cash and cash equivalents at July 1, 2010	<u>13,025,660</u>
Cash and cash equivalents at June 30, 2011	<u>\$ 5,613,356</u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 2,614,817
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	11,755
Changes in assets and liabilities:	
Reinsurance receivable	(38,049)
AHCCCS member care liabilities	(484,906)
Capitation and reconciliations due to/from AHCCCS	(322,700)
Accounts payable and accrued administrative expenses	<u>(32,766)</u>
Total adjustments	<u>(866,666)</u>
Net cash provided by operating activities	<u>\$ 1,748,151</u>
Supplemental disclosure:	
Interest paid	none

The accompanying notes are an integral part of this statement.

Cochise Health Systems

NOTES TO FINANCIAL STATEMENTS

June 30, 2011

NOTE 1 - GENERAL PLAN DESCRIPTION

The financial statements presented are for Cochise Health Systems (the Plan), which is a division of Cochise County Department of Aging and Social Services. No other County operations are included in these financial statements. The Plan is party to an Arizona Long-Term Care System (ALTCS) contract for Cochise County residents that was awarded to Cochise County on November 1, 1993, and the Graham and Greenlee Counties' ALTCS contracts that were awarded to Cochise County on December 13, 1999, and October 1, 2001, respectively. These contracts are administered under the auspices of the Arizona Health Care Cost Containment System (AHCCCS). The Plan provides acute medical care, long-term institutional care, and home and community based services for physically disabled and elderly persons who are AHCCCS members and are at risk of institutionalization.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Fund

A Fund is described as an independent fiscal and accounting entity with a self-balancing set of accounts used to record assets, related liabilities, reserves and equities which are segregated for the purpose of carrying on activities of the reporting entity.

Proprietary (Enterprise) Fund

This fund type is used to account for operations that are financed and operated in a manner similar to private business enterprises, in which the intent is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

Basis of Accounting

The financial statements were prepared using the accrual basis of accounting, following accounting principles U.S. generally accepted accounting principles as they apply to enterprise funds of state and local governments, and following the reporting guidelines as established by AHCCCS.

Cochise Health Systems

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2011

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTANT POLICIES – CONTINUED

Pronouncements of GASB and FASB

Government Accounting Standards Board (GASB) Statement No. 20 states that Financial Accounting Standards Board (FASB) and its predecessor body pronouncements issued before November 30, 1989, continue to be applicable to Enterprise Funds unless they conflict with or contradict GASB guidance.

Enterprise Funds may take either of the following approaches to FASB guidance issued subsequent to November 30, 1989.

1. An entity may elect to continue to follow FASB guidance that does not conflict with or contradict GASB guidance. If this election is made, it must be followed consistently. It would not be appropriate to follow some FASB pronouncements issued subsequent to the cutoff date, but not others.
2. An entity may elect not to subject itself to FASB guidance issued subsequent to the cutoff date. In that case, even FASB amendments of guidance issued prior to the cutoff date would not be applicable to proprietary operations.

The Plan has elected to subject itself to FASB guidance issued subsequent to November 30, 1989.

Use of Estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cochise Health Systems

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2011

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTANT POLICIES - CONTINUED

Cash and Cash Equivalents

For purposes of the statement of cash flows, the Plan considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. All of the Plan's monies are under the direct supervision of the Cochise County Treasurer's Office and were fully collateralized or invested in the Arizona State Treasurer's Local Government Investment Pool (LGIP).

Revenue Recognition

a. Capitation Revenue

The Plan receives capitation payments under the AHCCCS contract based on member months equivalents. At the beginning of each month, the Plan receives capitation based on the number of members enrolled for that month. As members are added or removed from enrollment, capitation is adjusted for the remaining portion of the month. At any given time, capitation may be due to or due from AHCCCS. Capitation revenue is recognized in the month that members are entitled to long-term and acute health care services. The Plan is required to provide those services to its members, regardless of the cost of care provided.

b. Reinsurance Revenue

The Plan is entitled to receive reinsurance revenue from AHCCCS for a percentage of costs incurred for in-patient hospital care and certain other medical expenses in excess of a stated deductible per member per contract year.

c. Share of Cost Adjustment

Per the contract with AHCCCS, members with income in excess of standards set by AHCCCS are to pay a portion of their covered expenses. This is known as a Share of Cost (SOC). A portion of the Plan's capitation is based on assumed SOC per member per month. If actual assigned SOC is less than assumed SOC, AHCCCS has agreed to reimburse the Plan. If actual assigned SOC is greater than assumed SOC, the Plan has agreed to reimburse AHCCCS. The SOC adjustment is based on current assigned SOC information from AHCCCS.

Cochise Health Systems

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2011

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTANT POLICIES - CONTINUED

Furniture, Equipment and Vehicles

Furniture, equipment and vehicles in excess of \$5,000 are recorded at cost and depreciated using straight-line and accelerated methods over the estimated useful lives of the assets ranging from 3-7 years.

Income Taxes

The Plan is a division of a governmental entity, and as such does not pay income taxes. Therefore, no provision for income taxes has been made in these statements.

Medical Expenses

All medical expenses are reported net of Medicare payments.

NOTE 3 - BONDING MECHANISM

On September 20, 1993, the Cochise County Board of Supervisors adopted Resolution 93-99 pledging to provide financial backing as an ALTCS program contractor, in the event of a default by the Plan. On November 22, 1999, the Cochise County Board of Supervisors adopted Resolution 99-80 amending Resolution 93-99 to include the addition of Graham County in the Cochise County ALTCS program service area. Effective October 1, 2001 Resolution 01-61 was adopted by the Board of Supervisors amending the previous resolutions to include Greenlee County.

NOTE 4 - RETIREMENT PLAN

Plan Description

The Plan contributes to the Arizona State Retirement System (ASRS), which administers a cost-sharing multiple-employer defined benefit pension plan that covers general employees of Cochise County. The ASRS is governed by the Arizona State Retirement System Board according to the provisions of A.R.S. Title 38, Chapter 5, Article 2. Benefits are established by state statute and generally provide retirement, death, long-term disability, survivor, and health insurance premium benefits.

Cochise Health Systems

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2011

NOTE 4 - RETIREMENT PLAN-CONTINUED

The ASRS issues a publicly available financial report that includes its financial statements and required supplementary information. A report may be obtained by writing or calling:

ASRS

3300 N. Central Avenue
P.O. Box 33910
Phoenix, AZ 85067-3910
(602) 240-2000 or (800) 621-3778

Funding Policy

The Arizona State Legislature establishes and may amend active plan members' and the Plan's contribution rates.

For the ASRS fiscal year ended June 30, 2011, active ASRS members and the Plan were each required by statute to contribute at the actuarially determined rate of 9.85 percent (9.6 percent retirement and 0.25 percent long-term disability) of the members' annual covered payroll. The Plan's contributions to ASRS for the years ended June 30, 2011, 2010 and 2009 were \$197,823, \$184,282, and \$175,615, respectively, which was equal to the required contributions for each respective year.

NOTE 5 – CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2011, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Furniture and equipment	\$ 45,093			\$ 45,093
Vehicles	113,614		\$ (36,683)	76,931
Less accumulated depreciation	(112,318)	\$ (11,755)	25,720	(98,353)
Total capital assets, net	<u>\$ 46,389</u>	<u>\$ (11,755)</u>	<u>\$ (10,963)</u>	<u>\$ 23,671</u>

Cochise Health Systems

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2011

NOTE 6 – CLAIMS PAYABLE

The Plan utilizes a computerized authorization system to aid in the determination of received but unpaid claims (RBUCs) and to prevent unauthorized services from being rendered. Providers are required to obtain authorization before services are rendered for most services provided. The Plan then uses historical analysis reports from their computer system to generate lag reports. These lag reports are used to estimate incurred but not reported claims (IBNRs). IBNRs are then added to RBUCs to determine claims payable. In addition, incentives of up to 2% of claims paid to institutional care providers can be earned and are accrued as claims payable.

Claims payable at June 30, 2011, consisted of the following:

Medical claims payable	\$ 3,021,700
Prior period coverage payable	5,000
Institutional care incentives	<u>40,000</u>
Total claims payable	<u>\$ 3,066,700</u>

NOTE 7 - RESTRICTED NET ASSETS

Per the contract with AHCCCS, the Plan is required to retain in equity an amount equal to \$2,000 per enrolled member at year-end. Restricted net assets totaled \$1,738,000 at June 30, 2011. The balance of any equity may be distributed after the issuance of the audited financial statements, with AHCCCS's permission. During the year ended June 30, 2011, the Plan transferred \$8,599,225 to Cochise County's general fund.

NOTE 8 - OTHER ADMINISTRATION

Following is a summary of other administration expenses for the year ended June 30, 2011:

Office supplies	\$ 23,151
Insurance	15,283
Minor equipment	11,655
Telephone	13,208
Travel and training	19,016
Dues and licenses	65,272
County overhead	706,617

Cochise Health Systems

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2011

NOTE 8 - OTHER ADMINISTRATION - CONTINUED

Postage	13,006
Printing	6,440
Consulting fees	50,653
Equipment lease	24,887
Other	<u>2,158</u>
	<u>\$ 951,346</u>

NOTE 9 - RELATED PARTY TRANSACTIONS

The Plan incurred administration fees from Cochise County of \$706,617 for the year ended June 30, 2011. At June 30, 2011, the Plan owed the County \$209,443. The Plan's employees are employees of the County and are subject to all rules and regulations of Cochise County.

NOTE 10 - RECONCILIATIONS RECEIVABLE FROM/(PAYABLE TO) AHCCCS

The amounts due from AHCCCS at June 30, 2011, are as follows:

Share of cost	<u>\$ 191,019</u>
---------------	-------------------

NOTE 11 - SUBSEQUENT EVENTS

The Plan received notice in May 2011 that its AHCCCS contract that expires in September 2011, would not be renewed. The contract provided 99% of the Plan's revenue during the year ended June 30, 2011. Therefore, starting in October 2011, the Division no longer is earning capitation revenue and will limit its operations to processing and paying claims. The Plan intends to continue paying authorized claims through September 30, 2012, in accordance with the contract.

The Plan has evaluated subsequent events through February 1, 2012, the date which the financial statements were available to be issued.